200419

SIDLEY & AUSTIN

A PARTNERSHIP INCLUDING PROFESSIONAL CORPORATIONS

CHICAGO
DALLAS
LOS ANGELES
NEW YORK

1722 EYE STREET, N.W.
WASHINGTON, D.C. 20006
TELEPHONE 202 736 8000
FACSIMILE 202 736 8711

FOUNDED 1866

HONG KONG
LONDON
SHANGHAI
SINGAPORE
TOKYO

WRITER'S DIRECT NUMBER
(202) 736-8198

WRITER'S E-MAIL ADDRESS
thynes@sidley.com

November 17, 2000

Honorable Vernon A. Williams
Secretary
Surface Transportation Board
Case Control Unit
1925 K Street, N.W.
Washington, D.C. 20423-0001

Re: STB Ex Parte No. 582 (Sub-No. 1); Major Rail Consolidation Procedures

Dear Mr. Williams:

Enclosed for filing in the above-captioned proceeding are the original and twenty-five (25) copies of Canadian Pacific Railway Company's Comments (CPR-4). Also enclosed is a computer disk containing a copy of this submission in WordPerfect format.

Please date-stamp the two (2) extra copies of the enclosed filing and return them via our messenger.

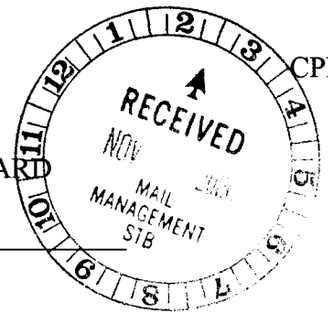
Sincerely,

Terence M. Hynes

Enclosures

cc: All Parties of Record

CPR-4



BEFORE THE
SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 582 (Sub-No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY REGARDING PROPOSED RAIL CONSOLIDATION REGULATIONS

Marcella M. Szel Q.C.
Canadian Pacific Railway Company
Suite 500, Gulf Canada Square
401 – 9th Avenue, SW
Calgary, AB T2P 4Z4
(403) 319-7000

Timothy G. Mulcahy
Canadian Pacific Railway Company
Suite 1000, Soo Line Building
105 South Fifth Street
Minneapolis, MN 55402
(612) 347-8325

Terence M. Hynes
Paul A. Hemmersbaugh
Sidley & Austin
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 736-8000
(202) 736-8711 (fax)

Counsel for Canadian Pacific Railway Company

DATED: November 17, 2000

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 582 (Sub-No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY
REGARDING PROPOSED RAIL CONSOLIDATION REGULATIONS

Pursuant to the Board's October 3, 2000 Notice of Proposed Rulemaking in the above-captioned proceeding (the *"NPR Order"*), Canadian Pacific Railway Company and its wholly-owned subsidiaries, Soo Line Railroad Company ("Soo"), Delaware and Hudson Railway Company, Inc. ("DHRC"), and St. Lawrence and Hudson Railway Company Limited ("St.L&H") (collectively "CPR") submit these initial comments concerning proposed modifications to the Board's Railroad Consolidation Procedures (49 C.F.R. §§ 1180.0–1180.9).

CPR agrees that it is appropriate to update the STB's merger regulations to take account of fundamental changes in the structure of the North American rail industry and the business environment in which railroads and their customers operate. The draft regulations propose a number of substantive changes that CPR supports. Most importantly, the proposed rules place a much greater emphasis on service quality and avoidance of the implementation-related service failures that have plagued recent Class I mergers. *See NPR Order* at 19-20, 35-37. CPR supports the proposed requirement that future applicants prepare a detailed "Service

Assurance Plan" as part of their application, and submit to STB oversight of the implementation process. These new rules will reduce the risk that future consolidations result in widespread service disruptions. The draft regulations also impose a heavier evidentiary burden on future applicants to show that their transaction would generate "substantial and demonstrable public benefits...." *NPR Order* at 11 (proposed § 1180.1(a)). CPR endorses the STB's intention to scrutinize claimed public benefits more rigorously, and to hold applicants accountable for delivering those benefits.

However, the proposed regulations relating to the Board's analysis of competition issues, and the "downstream" impacts of future consolidations, contain elements that are of significant concern to CPR. On the basis of unproven presumptions regarding the likely effects of future mergers on competition and service quality, the Board proposes to require all future applicants to offer measures to "enhance" rail-to-rail competition in their service territory. *See NPR Order* at 12-13 (proposed § 1180.1(c)). A universal requirement that merging carriers supplement the competitive choices of shippers – whether or not the record in a particular case demonstrates that such shippers would otherwise be harmed by the transaction – is incompatible with longstanding STB/ICC precedent and fundamental principles of administrative law. Moreover, the economic cost imposed by such a rule would discourage carriers from pursuing consolidations that might generate substantial public benefits without any unmitigated harm. Determinations with respect to possible negative effects of future mergers, and the necessity for conditions to mitigate or offset such effects, should be based on the evidence in each case – not on presumptions made before such transactions are even proposed.

Certain provisions in the draft regulations would require the parties to a merger case to engage in an excessive degree of speculation regarding future events. The draft regulation governing market impact analyses would require applicants to present "projected" market share data reflecting the effects of conditions imposed on their transaction, follow-on mergers and other post-merger developments that cannot be quantified with any degree of precision. *See NPR Order* at 32-34 (proposed § 1180.7(b)). Likewise, proposed § 1180.6(b)(12) would require applicants not only to predict what responsive transactions might follow their merger, but also to quantify the impact of such follow-on transactions on the net public benefits of their own merger, and to propose modified or additional conditions to address the supposed cumulative/crossover impacts of hypothetical future transactions. *See NPR Order* at 20-21, 31 (proposed §§ 1180.1(i), 1180.7(b)). The issues addressed by these provisions are important, and the Board should consider them in deciding whether to approve future merger applications. However, the level of detailed quantitative analysis required by the proposed regulations is simply not realistic, and could result in a record (and STB decisions) based upon an unacceptable degree of guesswork.

The following sections set forth CPR's position with respect to these and other important issues raised by the STB's proposed regulations.

I. SERVICE ISSUES

The proposed regulations devote far more attention to service issues than do the existing rules. The *NPR Order* indicates that the Board will weigh service quality more heavily

in estimating the benefits of a proposed merger, and will carefully scrutinize the potential for transitional service disruptions in evaluating possible merger harm. *NPR Order* at 11-15 (proposed §§ 1180.1(a), (c), (c)(1), (c)(2)). Proposed § 1180.10 would require future applicants to submit a detailed Service Assurance Plan "identifying the precise steps to be taken by applicants to ensure that projected service levels are attainable and that key elements of the operating plan will improve service." *NPR Order* at 35. Applicants would also be required to develop contingency plans for merger-related service disruptions, to establish problem resolution teams made up of interested stakeholders, and to submit to STB oversight of the implementation process. *NPR Order* at 19 (proposed § 1180.1(h)).

These new requirements are not only appropriate, they are absolutely necessary. Experience with recent rail mergers suggests that the most significant issues raised by future consolidation proposals are likely to be about service quality and reliability. The comments submitted during the earlier stages of this rulemaking proceeding confirm that the potential for future Class I mergers to disrupt the rail network is of vital concern to shippers. In light of this reality, the Board should scrutinize applicants' implementation plans carefully. In order to obtain approval for their merger, applicants should be required to demonstrate that they can implement their transaction without significant service failures.

However, CPR asks that the STB clarify its proposed rules relating to Service Assurance Plans in two respects:

First, proposed §§ 1180.10(a) and (c) contemplate analyses of anticipated service improvements based upon certain pre-merger service "benchmarks." Specifically, § 1180.10(a)

would require applicants to demonstrate how the merger would result in improved service levels using benchmarks "for **the year immediately preceding the filing date** of the application." It is not clear whether this language refers to the calendar year preceding the year in which the application is filed, or the twelve-month period immediately preceding the filing date of the application. It is doubtful whether performance statistics for the twelve months "immediately preceding the filing date" of a merger application would be readily available to applicants.[1] Proposed § 1180.10(c) incorporates a somewhat different timeframe, calling for benchmark analyses of dwell time and on-time performance for principal yards/terminals based upon information "for **one year prior to the transaction**." It is unclear how applicants would fix the date of "the transaction" for purposes of this provision. In order to provide clearer instruction regarding the benchmark data to be used by applicants, CPR suggests that the Board modify the language of both § 1180.10(a) and § 1180.10(c) to provide for the use of benchmark statistics "for the most recent twelve-month period for which data is available."

Proposed § 1180.10(i) would require applicants to develop contingency plans to deal with potential post-merger service failures. The regulation does not address the questions (1) when such contingency plans would be put into effect, and (2) who would make such a determination. It is appropriate for the STB to assure that merging carriers have effective contingency plans in place prior to consummating their transaction, and for the Board to oversee generally the implementation of approved mergers. However, regulatory micromanagement of

---

[1] Likewise, performance statistics for the full calendar year preceding the filing date might not be available if an application were filed in the early months of the year.

the implementation process – including determination of when to invoke contingency plans – is neither necessary nor practicable. CPR requests that the Board clarify that, while the STB will review applicants' contingency plans to assure that those plans deal effectively with potential service disruptions, it will not interject itself in the day-to-day process of implementing applicants' operating plan (including contingency plans).

II. PUBLIC BENEFITS

The proposed regulations contain several important provisions relating to the measurement of "public" benefits of rail mergers. First, the Board has stated that it plans to scrutinize claimed merger benefits more carefully to ensure that they are well-documented and reasonable. *NPR Order* at 14. Second, in order to discourage applicants from exaggerating the benefits of their transaction, the proposed regulations require them to "suggest additional measures that the Board might take if the anticipated public benefits identified by applicants fail to materialize in a timely manner." *NPR Order* at 31 (proposed § 1180.6(b)(11)); see *also NPR Order* at 14. Finally, the revised General Policy Statement indicates that, in future merger cases, the STB will accord increased weight to benefits stemming from enhanced competition and improved service, and less weight to carrier efficiency benefits. *NPR Order* at 12, 14.

In its prior comments, CPR urged the STB to subject public benefits calculations to more exacting scrutiny.[2] CPR also suggested that the Board encourage future applicants to

---

[2] *See* CPR-2, Comments of Canadian Pacific Ry. Co. at 18; CPR-3, Reply Comments of Canadian Pacific Ry. Co. at 15.

offer, on a voluntary basis, service guarantees or other remedies that would create an incentive for applicants to deliver the promised benefits of their transaction.[3] The proposed regulations adopt this voluntary approach, rather than creating new STB-supervised remedies (as advocated by certain parties).

While the proposed regulations do not explicitly incorporate new STB-sponsored remedies for post-merger service disruptions, shippers and short-line carriers might construe the reference to "additional measures" in § 1180.6(b)(11) as an invitation to seek conditions mandating such procedures in individual cases. The Board should clarify that § 1180.6(b)(11) is intended to encourage applicants to offer service guarantees or remedial procedures on a voluntary basis, but is not an indication that the Board itself will impose such remedies.

CPR also asks the Board to clarify that proposed § 1180.6(b)(11) is not intended to impede the ability of merging carriers to react appropriately to changing business conditions. Operating plans and capital spending proposals set forth in consolidation applications are based upon foreseeable circumstances at the time the application is filed. Changes in customer demand, unanticipated capital needs and competitive responses by other carriers might dictate that the merged carrier modify or postpone operating changes or investments identified as "public benefits" in the application, or pursue different (but perhaps equally beneficial) actions in the years immediately following the merger. A regulation that penalized the merged carrier for responding to changes in the business environment would not promote the public interest. The

---

[3] *See* CPR-3, Reply Comments of Canadian Pacific Ry. Co. at 6.

STB should not hamstring merging carriers by requiring them to adhere strictly to every element of their operating plan, or to implement their merger in precisely the manner described in the application. The "additional measures" contemplated by § 1180.6(b)(11) should be invoked only where the merger, as implemented, fails to deliver substantial public benefits.

III. COMPETITION ISSUES

The draft regulations propose a major change in the STB's policy with respect to competition issues in rail merger cases. Under the Board's existing regulations, a merger is approved if its public benefits outweigh any unmitigated competitive or other harm caused by the transaction. The Board has generally imposed conditions only to the extent necessary to preserve rail competition for shippers that would otherwise be rendered "captive" by the merger. *See* 49 C.F.R. § 1180.1. Proposed § 1180.1(c) would abandon this longstanding practice in favor of a policy under which applicants in all future cases would be required to "propose conditions that will not simply preserve but also enhance competition." *NPR Order* at 16 (proposed § 1180.1(d)).

The predicate for this radical shift in policy appears to be an assumption on the Board's part that **all** future Class I consolidations are likely to produce certain harmful effects. The Board expresses the view that "additional consolidation in the industry is .... likely to result in a number of anticompetitive effects, such as loss of geographic competition, that are increasingly difficult to remedy directly or proportionately." *NPR Order* at 12 (proposed

§ 1180.1(c)).[4] Notwithstanding its intention to scrutinize applicants' merger implementation plans much more closely, the Board finds that "[a]dditional consolidations could also result in service disruptions during the system integration period." *Id.*[5] Finally, the *NPR Order* reiterates the assumption that future Class I consolidations will not generate the same level of efficiency benefits as prior mergers. *Id.* at 11-12.

Based upon these presumed negative consequences of further industry consolidation, the Board concludes that "[t]o maintain a balance in favor of the public interest, merger applications must include provisions for enhanced competition." *NPR Order* at 12 (proposed § 1180.1(c)). Such competitive enhancements "need not be directed to remedying specific competitive or other harms that are threatened by the merger." *Id.* at 12. The Board suggests that applicants might satisfy this requirement by granting trackage rights, creating "shared or joint access areas," or by removing so-called "paper barriers" or "steel barriers" affecting connecting shortline carriers. *Id.* at 13. Thus, in order to win approval for a merger, future applicants must not only ***mitigate*** any anticompetitive impacts actually caused by their transaction, but must also supplement the level of rail-to-rail competition in their service territory

---

[4] The STB's renewed concern about product and geographic competition in its proposed merger regulations stands in stark contrast to the Board's decision to discontinue consideration of product and geographic competition in the market dominance phase of rate cases. *See Ex Parte No. 627, Market Dominance Determinations – Product and Geographic Competition* (served July 2, 1999).

[5] It is illogical to require conditions that permanently restructure the competitive balance as a means of offsetting temporary post-merger service failures. Indeed, introducing new operations by additional rail carriers on applicants' lines (particularly in terminal areas) during the implementation period would, if anything, increase the risk of congestion and service problems.

in order to ***offset*** a variety of adverse consequences that the regulations simply assume would flow from any such transaction.

CPR endorses the STB's stated objective of fashioning a merger policy that will "ensure balanced and sustainable competition in the railroad industry." *Id.* at 11 (proposed § 1180.1(a)). However, a rule that requires applicants in all cases to restructure the pre-merger competitive balance – without regard to whether the evidence demonstrates that such restructuring is needed to address any actual harm to the public – is unwarranted. The governing statute (49 U.S.C. § 11324) mandates only that the STB protect the public from any adverse competitive consequences of rail mergers. It does not require that all mergers affirmatively increase the level of rail-to-rail competition. The policy articulated in the proposed regulations represents a major departure from the Board's (and the ICC's) longstanding interpretation of the merger statute.[6]

The STB's blanket assumption that ***all*** future consolidations will reduce product and geographic competition and generate transitional service failures would appear to be inconsistent with administrative law governing agency presumptions. *See, e.g., National Mining Association v. U.S. Dep't of Interior*, 177 F.3d 1, 6 (D.C. Cir. 1999); *Secretary of Labor v. Keystone Coal Mining Corp.*, 151 F.3d 1096, 1100-01 (D.C. Cir. 1998). Inclusion of these

---

[6] The STB (and ICC) have consistently disfavored conditions that would broadly restructure the competitive balance among rail carriers. *See, e.g., Canadian National Ry. Co. et al. – Control – Illinois Central Corp., et al.* (served May 25, 1999) at 21-22; *Union Pacific Corp., et al. – Control – Missouri-Kansas-Texas Ry. Co., et al.*, 4 I.C.C.2d 409, 437 (1988); *Santa Fe Southern Pacific Corp. – Control – SPT Co.*, 2 I.C.C.2d 709, 827 (1986), 3 I.C.C.2d 926, 928 (1987).

presumptions in the Board's merger regulations is difficult to reconcile with the fundamental requirement that the Board's determinations in adjudicatory proceedings be based on substantial evidence in the record. *See, e.g., Landry v. FDIC*, 204 F.3d 1125, 1139 (D.C. Cir. 2000); *AT&T Corp. v. FCC*, 86 F.3d 242 (D.C. Cir. 1996); *see generally, United States v. ICC*, 296 U.S. 491 (1970); 5 U.S.C. § 706 (Administrative Procedure Act). While the Board's underlying concerns about these issues may be well-intentioned, the determination whether (and to what degree) a future consolidation would generate adverse effects of the type hypothesized in the proposed General Policy Statement must be made on a case-by-case basis.

Moreover, the assumption that future mergers will "enhance" competition only if the choices of shippers are supplemented through structural changes (such as trackage rights or shared terminal access) ignores the fact that mergers can promote competition in many ways. To the extent that a merger improves operational efficiency or strengthens applicants financially (particularly where the transaction would provide a solution to a weaker carrier's financial problems), consolidation can enhance the competitive capabilities of the rail system. By contrast, a regulation that requires merging carriers to grant competition-expanding concessions – even where such relief is not necessary to alleviate any reduction of competition caused by the merger – could impose prohibitive costs on prospective merger partners. The draft regulations afford little guidance regarding how much competitive enhancement would be "enough" to overcome the negative presumptions embodied in the rules. Concessions granted to one group of shippers would, in all likelihood, precipitate requests for similar treatment by others. It would be extremely difficult for the Board to articulate a consistent standard for determining when this

new requirement was met. The resulting uncertainty could lead the industry to forego transactions that would otherwise produce significant public benefits without harming competition.

Accordingly, CPR urges the Board to modify its proposed regulations relating to competition issues in several respects. In proposed § 1180.1(c) (1), the Board should delete the presumptions that future mergers are "likely" to result in anticompetitive effects and service disruptions, as well as the requirement that applicants "must include provisions for enhanced competition in all cases."[7] In place of those provisions, the Board can include language indicating that it will consider carefully, ***on a case-by-case basis***, the impact of future consolidations on product and geographic competition, and the likelihood that service may be disrupted during the implementation stage of the transaction. Proposed § 1180.1(d) could be revised to provide that, if the record shows that a particular merger would have adverse impacts that were not directly mitigated by conditions or offset by other demonstrable public benefits, voluntary measures by applicants to supplement the competitive choices of shippers would provide a means to satisfy the public interest balancing test. If a particular transaction would have detrimental effects that were not sufficiently mitigated or offset by applicants, the Board could either impose conditions to mitigate those effects or deny the application.

Revising the proposed regulations in this manner would assure that future merger cases are decided on the basis of record evidence, rather than unsupported assumptions. At the

---

[7] Corresponding revisions should also be made in proposed §§ 1180.1(c)(2) and 1180.1(d).

same time, the regulations would fairly apprise future applicants of the Board's intention to accord greater significance to potential effects of mergers on product and geographic competition and service quality. The proposed rules (so revised) would also make it clear that the Board would look favorably upon voluntary measures that increase the rail options of shippers as a means by which applicants might overcome adverse effects that cannot be mitigated directly. Finally, such an approach would be consistent with the STB's (and ICC's) longstanding preference for achieving public interest objectives through private industry initiatives rather than extensive regulation.

CPR also seeks clarification of proposed § 1180.1(c)(2)(ii), which provides that, in future merger proceedings, the STB "will consider whether projected shifts in traffic patterns could undermine the ability of the various network links (including Class II and Class III carriers and ports) to sustain essential services." The reference to ports is new, and suggests that the Board may, in future cases, assume that diversion of traffic from a U.S. port to a foreign port in connection with a cross-border rail merger is contrary to the public interest. Such an assumption would be contrary to the principles of NAFTA, which is intended to facilitate trade among the United States, Canada and Mexico. Consistent with NAFTA, the Board's decisions should

promote the development of an efficient continent-wide transportation system.[8] To the extent that diversion of traffic from a U.S. port to a Canadian port (or vice versa) results from more efficient single-system services offered by a transnational rail carrier, such diversion should be viewed as consistent with NAFTA, and with the overall public interest. By contrast, government action requiring – or prohibiting – such diversions would be contrary to the free trade principles articulated in NAFTA. CPR requests that the Board clarify that it will not exercise its authority over rail mergers in a manner that favors U.S. ports over their Canadian counterparts, but rather will evaluate the impact of port diversions on a case-by-case basis, and in a manner that takes into account the guiding principles of NAFTA.

The draft regulation governing Market Impact Analyses (proposed § 1180.7) imposes an unrealistic evidentiary burden on the parties to future consolidation cases. As currently drafted, it would require applicants to calculate "projected" post-merger market shares (including both traffic and revenues) for both rail carriers and other modes. *See* proposed § 1180.7(b)(2) and (3). It would be difficult for applicants to predict with any degree of certainty the market share likely to be captured by alternate rail carriers that were granted trackage rights or other conditions in conjunction with a merger. Follow-on mergers by other carriers, and any

---

[8] The Board has acknowledged that it has a "responsibility to ensure that [its] actions foster the goal of North American economic integration embodied in NAFTA." Docket No. AB-545, *South Orient R.R. Co. – Abandonment and Discontinuance of Trackage Rights* (served Oct. 6, 1998) ("*South Orient Abandonment*"). *See also* Finance Docket No. 32760, *Union Pac. Corp. et al – Control – Southern Pac. Rail Corp. et al.*, (Decision No. 44, served August 12, 1996) ("*UP/SP*") at 147 (same). The proposed regulations likewise recognize the STB's obligation to ensure that its decisions are consistent with NAFTA. *See NPR Order* at 21 (proposed § 1180.1(k)(2)).

conditions imposed in connection with those transactions, would also have a substantial impact on future traffic patterns. A number of external market factors, including plant openings/closures, changes in production or product demand, and changes in prices could also affect the future market shares of particular carriers. It is simply not realistic to expect applicants to forecast the impact of these events with any degree of precision. The Board should reconsider whether it is worthwhile to require applicants to engage in such guesswork.

The ability of future applicants to produce the types of market studies contemplated by the proposed regulation may also be limited by issues of data availability. Reliable and consistent data in the format contemplated by the draft regulations may not be readily available, particularly for non-rail modes. With respect to cross-border traffic, data limitations exist with respect to both rail and non-rail shipments. While CPR and CN submit data for inclusion in the STB's Waybill Sample, the growing number of provincial carriers in Canada do not. Moreover, the motor carrier data compiled by Statistics Canada is based upon a survey of major carriers, and does not include information regarding shipments handled by smaller carriers or private fleets. In order to take account of these (and other) potential shortcomings in available data, CPR suggests that the Board modify line 8 of proposed § 1180.7 to require that market impact analyses "provide the following types of information ***to the extent that it is available***...."

IV. "DOWNSTREAM" IMPACTS

CPR generally supports the STB's plan to assess the "downstream" implications of future rail mergers and, in particular, to consider the potential cumulative effect of another round of major transactions on the ultimate structure of the North American rail industry before allowing any one transaction to proceed.[9] However, the proposed regulations impose evidentiary requirements that are unduly burdensome, and which call for applicants and the Board to engage in an unacceptable degree of speculation about future events. Specifically, the regulations would require applicants to adjust the public benefits of their own merger to take account of the possible effects of hypothetical responsive consolidations. *NPR Order* at 31 (proposed § 1180.6(b)(12)(iii)). In addition, applicants would be required to discuss whether such conjectural follow-on transactions would require the Board to modify, or add to, the conditions imposed in connection with the first merger. *NPR Order* at 31 (proposed § 1180.6(b)(12)(ii)).[10]

In the absence of an actual responsive merger proposal (and an STB application filed by the parties to that transaction), any attempt by applicants in the first proceeding to develop the detailed quantitative evidence contemplated by §§ 1180.6(b)(12)(ii) and (iii) would

---

[9] Under the proposed regulations, future applicants would be required to "anticipate with as much certainty as possible what additional Class I merger applications are likely to be filed in response to their own application," and to explain how their merger and any responsive transactions "could affect the eventual structure of the industry and the public interest." *NPR Order* at 20 (proposed § 1180.1(i)). *See also id.* at 31 (proposed § 1180.6(b)(12)).

[10] In addition to these explicit requirements, the proposed regulations also appear to require applicants to account for the effects of hypothetical responsive mergers in calculating "projected" market share data pursuant to proposed § 1180.7.

be fraught with speculation and the potential for error. In order to comply with these provisions, applicants would have to predict not only which carriers might merge in response to their transaction, but also when such transaction(s) would be proposed, approved, consummated, and implemented. Even if applicants could accurately predict the timing of those events, they would lack detailed information (at the time they filed their application) regarding critical elements of the responsive merger, including (1) the precise structure of the transaction; (2) the operating plans and marketing strategies of the merging carriers; (3) any new services and facilities investments that might be proposed as part of the responsive application; (4) what competitive or other conditions might be proposed by (or imposed upon) the follow-on merger applicants; and (5) the likely reaction of shippers to the service offerings of the hypothetical merged carrier. This information would be essential for applicants in the first merger proceeding to quantify in any meaningful fashion the impact of the responsive merger on the projected benefits of their own consolidation, or to address the question whether conditions imposed in the first merger would need to be modified, supplemented or revoked as a result of the second transaction. Yet, unless a follow-on merger were actually proposed, applicants would be required to speculate, without foundation in concrete facts or data, about each of these important issues.[11] "Quantitative" evidence based upon such compound speculation would be, at best, of

---

[11] If a responsive merger application were actually filed while the first consolidation was before the Board, applicants in the first proceeding could utilize that application (and the evidentiary record in the latter case) as a basis for addressing the issues raised by proposed § 1180.6 (b)(12). Indeed, depending upon the timing of the follow-on transaction, the Board could either consolidate the proceedings for evidentiary purposes, or request supplemental filings in the first proceeding.

questionable validity. STB decisions based on such material would be vulnerable to legal attack as supported only by speculation, rather than substantial evidence. *See, e.g., Landry v. FDIC*, 204 F.3d 1125, 1139 (D.C. Cir. 2000); *AT&T Corp. v. FCC*, 86 F.3d 242 (D.C. Cir. 1996); *see generally*, 5 U.S.C. § 705-706.

Moreover, proposed §§ 1180.6(b)(12)(ii) and (iii) would have a number of undesirable practical effects on the conduct of future consolidation cases. In order to obtain the information required by those provisions, merger applicants would, no doubt, seek discovery of other Class I carriers' internal studies or Board of Directors presentations regarding possible merger partners or the potential benefits of various consolidation transactions. Railroad CEO's would be pressed in depositions to divulge information regarding their discussions with other carriers concerning merger or other joint strategic ventures. Exposing a non-applicant carrier's ongoing business deliberations to discovery by its competitors would have a serious chilling effect on the ability of carriers to pursue strategic initiatives on a confidential basis. In the past, the Board (and the ICC) have been loathe to permit extensive discovery regarding such sensitive issues. However, the evidentiary requirements of proposed §§ 1180.6(b)(12)(ii) and (iii) might open these topics to discovery in future cases. Premature disclosure of merger negotiations during the STB discovery process could also raise difficult issues under the securities laws. Even if such discovery were not permitted, a requirement that applicants quantify the impacts of hypothetical future mergers, and that other parties respond to such speculative evidence, would unduly complicate and prolong future consolidation cases.

For these reasons, CPR requests that the Board reconsider proposed §§ 1180.6(b)(12)(ii) and (iii). The burden associated with any attempt to "fine tune" applicants' benefits calculations to account for the effects of hypothetical transactions, and the highly speculative nature of the resulting evidence, outweigh the probative value of such an exercise. Accordingly, CPR believes that proposed § 1180.6(b)(12)(iii) should be deleted. With respect to § 1180.6(b)(12)(ii), the Board should require only that applicants explain whether any conditions proposed by them (or imposed by the Board) would likely require modification if a follow-on merger were to come to pass. However, the public would be best served if the Board deferred decision concerning such modifications until the actual facts relating to responsive consolidation proposals are known. Likewise, applicants and other parties should not be required to fashion "springing" conditions to be imposed on account of unannounced future consolidations. The Board can utilize the second merger proceeding, and its oversight of the first consolidation, to address these issues.

V. TRANSNATIONAL TRANSACTIONS

The Board takes note of the fact that future Class I mergers may include transactions between the major U.S. railroads and their Canadian or Mexican counterparts, and suggests that such transactions may raise "novel" issues. *NPR Order* at 21. The draft regulations explicitly recognize that the Board's decisions in such proceedings must be "consistent with the North America Free Trade Agreement and other pertinent international agreements to which the United States is a party." *Id.* (proposed § 1180.1(k)). To that end, the Board indicates that, in

deciding transnational merger cases, it will cooperate with Canadian and/or Mexican government agencies that are charged with reviewing the transaction, and will consult with "relevant officials" to assure that the Board's determinations are in harmony with NAFTA. *Id.* (proposed § 1180.1(k)(2)).[12]

The proposed regulations require that applicants in future transnational merger cases submit "full system" operating plans and competitive analyses reflecting operations both within and outside of the United States. *See NPR Order* at 21 (proposed § 1180.1(k)(1)). CPR supports this requirement.

However, proposed § 1180.1(k)(1) contains certain additional provisions that would impose unique evidentiary burdens on "foreign" applicants. These nationality-based requirements conflict with the trade policies embodied in NAFTA. Chapter 11 of NAFTA expressly prohibits discrimination between U.S. and Canadian parties in connection with corporate control and investment transactions. Specifically, Article 1102 of NAFTA requires the United States to accord Canadian investors:

> treatment no less favorable than it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

NAFTA Article 1102(1) (emphasis added). *See also* NAFTA Article 1106 (prohibiting the U.S. from imposing discriminatory performance requirements relating to Canadian acquisition or

---

[12] CPR urges the Board to include relevant officials of both the United States and Canada in any consultations involving a U.S.-Canada rail merger, so that the perspectives of both nations on NAFTA-related issues are taken into account.

operation of investments in the U.S.); Article 1202 (requiring the U.S. to accord Canadian service providers, ***including transportation providers***, treatment no less favorable than it accords to its own service providers). Thus, NAFTA allows U.S. government agencies to impose application requirements and standards on Canadian (or Mexican) applicants ***only*** to the extent that such requirements and standards apply to U.S. applicants as well.

Proposed § 1180.1(k)(1) would require non-U.S. applicants to "explain how cooperation with the [FRA] will be maintained without regard to the national origins of merger applicants." It is entirely appropriate for the Board to ensure that merger applicants can – and will – comply with all applicable FRA safety regulations in operating lines located within the United States. However, it would be discriminatory for the Board's merger regulations to require only "foreign" applicants (and not their U.S. counterparts) to make such a showing in their application. Moreover, it would be improper for the Board to require non-U.S. applicants to take any action that is not required of U.S. railroads under U.S. laws or regulations, or to refrain from taking any action that is not prohibited by such laws or regulations. A rule that imposed such unique additional obligations on non-U.S. applicants would violate NAFTA policies. If the Board decides to retain this provision in the final merger rules, it should be made applicable to all future applicants. The Board should also make it clear that the provision requires carriers ***only*** to comply with U.S. law as written, and not to "cooperate" with FRA requests that they conduct their operations in ways that are not required (or prohibited) by U.S. laws or regulations.

Proposed § 1180.1(k)(1) further provides that "[w]hen an application would result in foreign control of a Class I railroad, applicants must assess the likelihood that commercial

decisions made by foreign railroads could be based on national or provincial rather than broader economic considerations and be detrimental to the interests of the United States rail network...." *NPR Order* at 21 (proposed § 1180.1(k)(1)). This additional nationality-based requirement, not imposed on U.S. Class I applicants, is precisely the sort of discrimination against Canadian firms that NAFTA proscribes. Like their U.S. counterparts, the Canadian Class I carriers are private corporations owned and controlled by their shareholders, ***not*** by any governmental entity.[13] Their managements have the same fiduciary obligation as U.S. railroad managements to promote the interests of the company's stockholders, not to pursue the agenda of any government. It is no more logical to suggest that CPR's management might make decisions regarding matters such as the siting of new facilities, the allocation of equipment during periods of peak demand, or rate levels in a manner that placed the wishes of Canadian or provincial governments above CPR's own economic interests than it would be to assume that a carrier such as BNSF would favor the interests of Texas (BNSF's home state) over its own commercial interests in making the same decisions. Indeed, if CPR or CN were to acquire control of any one of the major U.S. Class I railroads, the great majority of the resulting system's lines would be located in the United States, rather than Canada. In such circumstances, it would be even less conceivable that the Canadian firm would act in a manner "detrimental to the interests of the United States rail network...." *NPR Order* at 21 (proposed § 1180.1(k)(1)).

---

[13] In fact, the majority of the shares of CPR's parent, Canadian Pacific Limited, are owned by U.S. stockholders. The majority of CN's common stock is likewise held by U.S. citizens. *See Comments of Canadian National Ry. Co.* (served May 16, 2000) at 48.

Both CPR and CN have operated U.S. rail lines for more than a century, and each acquired a U.S. rail carrier during the past decade. At no time has any party suggested (much less demonstrated) that CPR or CN has placed the interests of a foreign government over its own commercial interests, or otherwise operated its U.S. properties in a manner detrimental to the public interest. There is no legitimate legal or factual basis for imposing upon non-U.S. applicants the unique evidentiary burden of showing that their commercial actions would be based upon economic self-interest rather than the wishes of a foreign government. CPR strongly urges the Board to delete this requirement from its final merger regulations.[14]

VI. OTHER ISSUES

In the *NPR Order*, the Board reiterates its preference for negotiated (rather than litigated) solutions to labor issues arising from rail mergers. The Board urges the major Class I railroads and their unions to reach voluntary agreements governing merger-related disputes in order to obviate the need for STB intervention. Yet, proposed § 1180.1(e) indicates that the Board intends to "review negotiated agreements to assure fair and equitable treatment of all affected employees." *NPR Order* at 17.

The STB's proposal to review negotiated labor agreements to assure their "fairness" is inappropriate. This procedure would create a risk that individual employees, or

---

[14] Proposed § 1180.1(k)(1) would also require foreign applicants to "address how any ownership restrictions imposed by foreign governments should affect our public interest assessment." CPR takes no position with respect to this provision, which would not apply to CPR (whose stock is not subject to any such restriction).

groups of employees, might challenge the terms of agreements negotiated by their unions in an effort to persuade the STB to "sweeten" those deals, or to "match" the terms of agreements entered into by applicants (or by different carriers and labor organizations) in other merger cases. Such a result would create a disincentive for carriers to enter into voluntary agreements with employees.

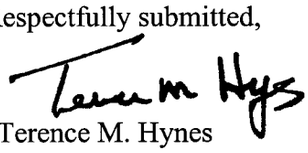
Proposed § 1180.6(b)(9) would require that the Employee Impact Exhibit include effects on applicant carrier employees located outside the United States. *NPR Order* at 30. In imposing this requirement, the Board concluded that its evaluation of future cross-border mergers will "require knowledge, on our part, of the effects of the proposed transaction upon all applicant carriers' employees, regardless of whether they are located in Canada, Mexico or elsewhere." *Id.* at 30. While it is reasonable for the STB to seek "full system" labor impact information for purposes of understanding the overall effects of a cross-border transaction, the filing of such data could motivate non-U.S. employees to petition the STB for compensation or other relief to mitigate harms they might experience as a result of the merger. CPR requests that the Board clarify that this informational requirement is not intended to signal an assertion of jurisdiction by the Board over the extraterritorial labor impacts of future transnational mergers, and that potential impacts of such transactions on Canadian (or Mexican) employees remain the sole province of Canadian (or Mexican) law.

Finally, the regulation governing the filing of applicants' Notice of Intent has been expanded in several significant respects. Applicants would be required to file a proposed procedural schedule and protective order simultaneously with the Notice of Intent. *NPR Order* at 25 (proposed § 1180.4(b)(4)(i) and (ii)). In addition, applicants would be required to make their 100% traffic tapes available to any interested party "as soon as practicable" following the Notice of Intent. *Id.* (proposed § 1180.4(b)(4)(iii)).[15] Where a voting trust would be used to consummate an acquisition of shares prior to STB approval, applicants would be required to submit the proposed voting trust agreement with their Notice of Intent, along with a statement demonstrating that the agreement would effectively insulate them from unlawful control of the acquired entity during the STB review process. Interested parties would have an opportunity to comment on the effectiveness of the voting trust agreement. *Id.* (proposed § 1180.4(b)(4)(iv)). Finally, proposed § 1180.4(b)(4) would abolish the procedural deadlines in current § 1180.4, in favor of a "customized" procedural schedule (as has been the practice in recent Class I merger

[15] In past cases, applicants have generally refused to provide traffic tapes until after the application was filed, citing the prohibition on discovery until that time.

cases). CPR endorses these proposed changes, which would provide a more orderly and uniform method for handling preliminary procedural issues in future consolidation cases.

Respectfully submitted,



Terence M. Hynes
Paul A. Hemmersbaugh
Sidley & Austin
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 736-8000
(202) 736-8711 (fax)

Marcella M. Szel Q.C.
Canadian Pacific Railway Company
Suite 500, Gulf Canada Square
401 – 9th Avenue, SW
Calgary, AB T2P 4Z4
(403) 319-7000

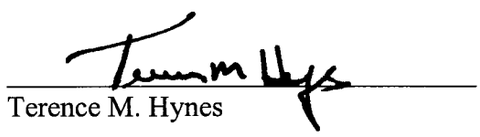
Timothy G. Mulcahy
Canadian Pacific Railway Company
Suite 1000, Soo Line Building
105 South Fifth Street
Minneapolis, MN 55402
(612) 347-8325

Counsel for Canadian Pacific Railway Company

DATED: November 17, 2000

CERTIFICATE OF SERVICE

I hereby certify that, on this 17th day of November, 2000, I served the foregoing Comments of Canadian Pacific Railway Company by messenger or postage prepaid, first class mail upon all known parties of record.



Terence M. Hynes